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SUBJECT: PERU SECTION 1377 TELECOM REVIEW

REF: STATE 1035

SUMMARY

¶1. (U) Per reftel, Econoff provided Peruvian telecom regulator OSIPTEL with NII Holdings' (Nextel) public comments and informed OSIPTEL of USTR's deadline for voluntary replies. As a follow-up, Econoff met with OSIPTEL's Manager for Regulatory Policies and Strategic Planning Jose Gallardo and seven other OSIPTEL representatives on January 16 to inquire whether the GOP had plans to reevaluate the current three-year maximum mobile termination rate (MTR) reduction scale, highlighting the concerns laid out by Nextel. Gallardo responded that OSIPTEL does not plan to review MTRs until 2009, after the current gradual reductions are complete. He explained that other mobile providers opposed MTR reductions, that Nextel had recommended a three-year approach, and that the mobile telecom sector in Peru was growing well. End Summary.

OSIPTEL'S PERSPECTIVE

¶3. (SBU) Gallardo explained that in its November 2005 decree, OSIPTEL decided upon a gradual maximum MTR reduction scale as a balanced way to address industry's diverging business models. According to Gallardo, TIM (now America Movil) wanted increased MTRs, Telefonica (the dominant provider) wanted to maintain existing rates, and Nextel wanted rates cut. While the advantages of lowering rates was clear, OSIPTEL also recognized that higher rates encouraged infrastructure investments in under-served geographic areas, a key GOP priority. Therefore, OSIPTEL announced that the 2005 average MTR of USD 0.2053 would be lowered to 0.1782 in January 2006, 0.1511 in January 2007, 0.1240 in January 2008, and 0.0969 in January 2009. If dissatisfied with the decree, industry had the option to request "administrative reconsideration" as well as to pursue judicial action within three months. According to Gallardo, Nextel did not pursue either option. On the other hand, Telefonica did pursue the judicial course in an effort to stop the reductions, but, after considering opinions submitted by Nextel and others, the court upheld the reductions.

¶4. (SBU) Gallardo also provided Econoff a copy of a letter from Nextel to OSIPTEL dated March 2, 2005, through which Nextel submitted a report on MTRs done by Analysis Consulting to support Nextel's efforts to get OSIPTEL to reduce MTRs. In the section entitled "Best-Practice Considerations in Reducing MTRs," the report said, "it would be inadvisable to implement adjustments to (MTR) costs in their entirety immediately or over the very short term... even in markets

where the discrepancy between cost and current rates is less significant than in Peru, regulators proposing cost orientation have generally adopted medium-term price controls and limited initial reductions in rates... in the UK, for example, a three-year glide path was used." In its conclusion, the report recommended that OSIPTEL use a three-year glide path for reducing MTRs.

15. (U) Finally, Gallardo noted that OSIPTEL's policies seemed to be positively affecting the mobile telecom market. He said there were 8.9 million mobile lines in 2006, compared with 2.93 million in 2003, 4.09 million in 2004, and 5.58 million in 2005. He also noted that new lines had stagnated at under 300 million per quarter from the last quarter in 2003 until the third quarter of 2005, but have skyrocketed since then (when OSIPTEL issued the decree), reaching 1.326 billion new lines in the fourth quarter of 2006. Gallardo was also pleased that the number of geographic districts in Peru with mobile coverage has more than doubled from 434 in December 2005 to 983 in December 2006.

POST COMMENT

16. (SBU) The November 2005 decree establishing a three-year gradual reduction in MTRs was an important step towards improving competition in the mobile telecom market and reducing costs for users. Before the reform, dominant provider Telefonica charged the highest MTRs; with the reform, competitors Nextel and America Movil can now charge higher rates than Telefonica. OSIPTEL overcame stiff challenges from Telefonica in enacting these decreases, and selected the three-year approach in part because of information provided by Nextel. There were even media accusations of undue USG influence on OSIPTEL, causing them to favor Nextel's views over Telefonica's.

17. (SBU) That said, there are currently only three mobile telecom providers in Peru, and the current average maximum MTR in Peru (USD 0.1511 as of January 1, 2007) is still above the regional average and above cost. Post feels that in the current environment, it is unlikely that OSIPTEL can be convinced to accelerate MTR reductions before January 2009. If the pending U.S.-Peru Trade Promotion Agreement (PTPA), referred to in NII Holdings' filing, is approved by the U.S. Congress, it may be possible to seek additional MTR reductions as the agreement calls for "reasonable rates." Furthermore, the GOP is in the process of selecting a new head of OSIPTEL, which will also likely lead to staffing changes throughout the organization. Nextel might be able to convince the new OSIPTEL team to consider further MTR reductions.

POWERS